

## Message Text

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LIMDIS

E.O. 11652: GDS

TAGS: ETRD, US, CH

SUBJECT: PROBLEMS AND PROSPECTS IN SINO-US TRADE

SUMMARY. SINO-US TRADE IN 1974 REGISTERED AN IMPRESSIVE GAIN OVER 1973, BUT IF FELL BELOW EARLIER EXPECTATIONS AND IS EXPECTED TO DECLINE SIGNIFICANTLY IN 1975. NUMEROUS PROBLEMS HAVE ARISEN FOR WHICH THE REASONS ARE MANIFOLD. THE DECLINE IN US AGRICULTURAL SALES TO CHINA SEEMS PRIMARILY DUE TO ECONOMIC AND OTHER

JUSTIFIABLE FACTORS. HOWEVER, IN THE CASE OF INDUSTRIAL EQUIPMENT CHINESE PURCHASES HAVE BEEN HIGHLY SELECTIVE, AND THERE IS SOME EVIDENCE OF DISCRIMINATION AGAINST US FIRMS FOR REASONS WHICH APPEAR TO BE POLITICAL. IN THIS CABLE, USLO EXAMINES THE MAJOR PROBLEMS IN SINO-US TRADE OVER THE LAST YEAR AND THE OUTLOOK FOR THE FUTURE, WHICH IS NOT AS BOURGANT AS IT SEEMED ONE YEAR AGO.

WE BELIEVE THIS FUTURE WILL WITNESS DIMINISHED SALES OF US AGRICULTURAL COMMODITIES. THE TCK PROBLEM VIRTUALLY INSURES THAT THE US WILL BE NO MORE THAN A RESIDUAL SUPPLIER OF WHEAT, AND PROBLEMS WHICH DEVELOPED LAST YEAR SEEM TO RULE OUT FUTURE SALES OF CORN AND SOYBEANS. THERE ARE GOOD LONG TERM PROSPECTS FOR

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AMERICAN COTTON, BUT WEAKENED FOREIGN DEMAND FOR CHINESE

TEXTILES WILL TEMPORARILY AFFECT US SALES. THE OUTLOOK FOR US PLANT AND EQUIPMENT REMAINS EXCELLENT OVER THE LONG TERM, BUT HOW MUCH PROGRESS WILL BE MADE IN THE SHORT TERM IS UNCERTAIN. IT IS POSS-

IBLE, HOWEVER, THAT REDUCED AGRICULTURAL IMPORTS FROM THE US WILL BE ACCOMPANIED BY A GREATER CHINESE WILLINGNESS TO BUY AMERICAN INDUSTRIAL GOODS. THERE IS GOOD LONG TERM POTENTIAL FOR SALES OF STEEL SCRAP. ON THE CHINESE EXPORT SIDE, PRC SALES TO THE US SHOULD CONTINUE TO SHOW GOOD INCREASES, BUT THE TRADE IMBALANCE IS LIKELY TO REMAIN LARGE, UNLESS PURCHASES FROM THE US ARE DRASTICALLY REDUCED OR UNLESS CHINESE OIL COMES INTO THE PICTURE. END SUMMARY.

1. INTRODUCTION: WHILE FINAL FIGURES ARE NOT YET IN, SINO-US TRADE IN 1974 REGISTERED AN IMPRESSIVE GAIN OVER 1973, FROM \$753 TO ABOUT \$930 MILLION. HOWEVER, DUE TO CHINESE CANCELLATIONS AND REQUESTS FOR DELIVERY DELAYS OF US AGRICULTURAL COMMODITIES, THE 1974 FIGURE FELL SEVERAL HUNDRED MILLION DOLLARS SHORT OF EARLIER EXPECTATIONS. MOREOVER, THE LEVEL OF TRADE IS EXPECTED TO DECLINE SIGNIFICANTLY IN 1975, TO BETWEEN \$600 AND \$700 MILLION, PRIMARILY THE RESULT OF A LOWER LEVEL OF CHINESE AGRICULTURAL PURCHASES.

2. THE LAST YEAR WITNESSED SERIOUS PROBLEMS IN CHINESE PURCHASES OF US AGRICULTURAL COMMODITIES, SLOW PROGRESS IN NEGOTIATIONS FOR, OR SALES OF, US PLANT AND EQUIPMENT, AND LITTLE FORWARD MOTION IN THE "ATMOSPHERICS" OF SINO-US TRADE, SUCH AS EXCHANGES OF TRADE MISSIONS. THE REASONS FOR THESE AND OTHER BILATERAL TRADE PROBLEMS ARE MANIFOLD, AND IT IS MOST DIFFICULT TO GIVE EACH FACTOR ITS PROPER WEIGHT. THE DISAPPOINTING TURN OF EVENTS SEEMS PRIMARILY DUE TO A VARIETY OF PLAUSIBLE COMMERCIAL AND ECONOMIC FACTORS. BUT SUCH FACTORS FAIL TO PROVIDE THE WHOLE ANSWER, AND TO SOME EXTENT CHINESE ATTITUDES AND ACTIONS ON TRADE WITH THE US APPEAR TO HAVE BEEN AFFECTED BY POLITICAL CONSIDERATIONS. THIS CABLE IS AN EFFORT TO PUT THE THE MATTER SOME PERSPECTIVE.

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3. PROBLEMS IN EXPORT OF US AGRICULTURAL COMMODITIES:

THE MAIN FACTOR IN SINO-US TRADE HAS BEEN CHINESE PURCHASES OF US AGRICULTURAL COMMODITIES, WHICH HAVE COMPRISED 80-85 PERCENT OF US EXPORTS AND, SINCE US IMPORTS ARE SO SMALL, A SLIGHTLY LOWER PERCENTAGE OF THE TWO-WAY TRADE. IT IS THESE PURCHASES WHICH

HAVE COMPRISED 80-85 PERCENT OF US EXPORTS AND, SINCE US IMPORTS ARE SO SMALL, A SLIGHTLY LOWER PERCENTAGE OF THE TWO-WAY TRADE. IT IS THESE PURCHASES WHICH ACCOUNT FOR THE PHENOMENAL GROWTH OF SINO-US TRADE FROM 1972 TO 1974, AND LIKEWISE, FOR THE LOWER THAN PREDICTED RESULTS IN 1974, AND THE EXPECTED DECLINE IN 1975.

4. TO A VERY GREAT EXTENT THE TREND OF THESE PURCHASES, BOTH UP AND DOWN, HAS BEEN A FUNCTION OF THE CHINESE DOMESTIC AGRICULTURAL SITUATION. FOR EXAMPLE, CHINESE GRAIN IMPORTS FROM ALL SOURCES ROSE SHARPLY AFTER THE DISAPPOINTING HARVEST OF 1972, AND THE US WAS A BENEFICIARY OF THESE GREATLY INCREASED PURCHASES WHICH NORMALLY HAVE BEEN CONCENTRATED IN CANADA AND AUSTRALIA. THE CUTBACK OF GRAIN DELIVERIES IN 1974, AND AN EXPECTED DECLINE IN 1975, SIMILARLY ARE ATTRIBUTABLE TO CHINA'S IMPROVED AGRICULTURAL PERFORMANCE, ALTHOUGH OTHER FACTORS ARE AT PLAY. THESE INCLUDE PORT CONGESTION PROBLEMS AND FOREIGN EXCHANGE DIFFICULTIES WHICH HAVE CAUSED THE CHINESE TO SEEK POSTPONEMENTS OF COMMODITY AND OTHER SHIPMENTS TO CHINA FROM VARIOUS SUPPLIERS. IN THIS RESPECT, SUPPLIERS OF US WHEAT WERE ASKED IN SEPTEMBER TO DELAY SOME OF THE 1974 SCHEDULED WHEAT SHIPMENTS TO 1975.

5. THERE HAVE ALSO BEEN SPECIAL PROBLEMS OF CHINESE DISSATISFACTION WITH THE QUALITY OF US AGRICULTURAL COMMODITIES. MOST IMPORTANT IS THE PRESENCE IN MUCH OF US WHEAT OF TCK SMUT WHICH THE CHINESE STRICTLY PROHIBIT FROM IMPORT. THE CHINESE ALSO COMPLAINED ABOUT HIGH MOISTURE CONTENT, RESULTANT MOLD, AND FOREIGN MATTER IN US CORN, AND POISONOUS DATURA SEEDS IN US SOYBEANS. IN THE CASE OF CORN AND SOYBEANS, THEY CANCELLED OR SOLD BACK LARGE OUTSTANDING ORDERS. THERE WERE NO CANCELLATIONS OF WHEAT CONTRACTS, BUT THE TCK PROBLEM WILL UNDOUBTEDLY AFFECT FUTURE PURCHASES.

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6. WE DO NOT DOUBT THE SINCERITY OF THE CHINESE COMPLAINTS, ALTHOUGH THE CAMPAIGN IN 1974 CRITICISING OVER-RELIANCE ON IMPORTS AND OFFICIALS WHO EVEN ACCEPT "GOTTEN" FOREIGN GOODS, MAY HAVE CONTRIBUTED TO THE RIGIDITY OF THE CHINESE NEGOTIATING POSITION. THE PROBLEM OF TCK REACHED A CRISIS POINT IN THE SPRING OF 1974, AFTER A YEAR OF COMPLAINTS TO THE SUPPLIERS, AND AFTER PRELIMINARY EFFORTS TO PREVENT TCK CARGOES FROM REACHING CHINA WERE UNSUCCESSFUL. ONLY WHEN THESE EARLIER ATTEMPTS AT RESOLUTION HAD FAILED DID THE CHINESE REFUSE TO ACCEPT FURTHER INFECTED CARGOES, BRINGING SHIPMENTS TO A HALT. THROUGHOUT THE SPRING IMPASSE, THE CHINESE STRESSED THEIR NEED FOR WHEAT, BUT WITHOUT TCK. AFTER A "GENTLEMEN'S AGREEMENT" WAS REACHED, SHIPMENTS RESUMED AND THE CHINESE IMMEDIATELY PURCHASED AN ADDITIONAL 600 THOUSAND TONS. IN THE CASE OF CORN, TRADERS ACKNOWLEDGE THAT THERE WERE CHINESE COMPLAINTS FROM THE TIME

US SHIPMENTS BEGAN TO ARRIVE. WE HAVE LESS INFORMATION ON THE SOYBEAN PROBLEM, BUT NO REASON TO BELIEVE IT WAS A BOGUS ISSUE. THESE PROBLEMS SEEMED TO STEM FROM THE USE OF CORN FOR HUMAN CONSUMPTION INSTEAD OF FEED, AND THE INAPPROPRIATE GRADE OF SOYBEANS FOR MAKING BEAN CURD. IN BOTH CORN AND SOYBEANS, MARKET CONDITIONS WERE SUCH THAT THE CHINESE DID NOT NEED EXCUSES IF THEIR OBJECTIVE WERE SIMPLY TO GET OUT OF EXISTING CONTRACTS.

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7. AS FOR THE FUTURE, THE CHINESE APPARENTLY DO NOT INTEND TO BUY US CORN OR SOYBEANS AGAIN, BUT THIS IS LESS IMPORTANT THAN THE WHEAT PROBLEM SINCE THE CHINESE DO NOT ORDINARILY IMPORT SIGNIFICANT QUANTITIES OF THOSE COMMODITIES. NOTWITHSTANDING THE "GENTLEMEN'S AGREEMENT," THE TCK PROBLEM VIRTUALLY INSURES THAT THE US WILL BE LIMITED TO BEING A RESIDUAL SUPPLIER, AFTER CANADA AND AUSTRALIA. BECAUSE OF THE TROUBLE INVOLVED WHEN TCK CARGOES ARRIVE (THERE WERE TWO IN THE LATTER HALF OF 1974), THE CHINESE WILL PRESUMABLY REMAIN RELUCTANT TO ORDER US WHEAT. MOREOVER, THE SELLERS ARE FORCED TO QUOTE HIGHER PRICES FOR CHINA IN ORDER TO COVER THEIR OWN TCK RISKS (E.G. TO DIVERT INFECTED SHIPMENTS TO OTHER DESTINATIONS OR TO

REIMBURSE THE CHINESE FOR STERILIZATION). THUS THE HUGE CHINESE PURCHASES OF THE LAST YEAR AND A HALF ARE NOT LIKELY TO RECUR EXCEPT IN YEARS OF UNUSUAL CHINESE DEMAND AND TIGHT WORLD SUPPLIES. FORTUNATELY, THERE HAVE BEEN NO SERIOUS PROBLEMS WITH US COTTON, WHICH SHOULD CONTINUE TO BE AN IMPORTANT EXPORT TO CHINA. TO HELP SUSTAIN GROWING TEXTILE EXPORTS, THE PRC HAS BEEN A LARGE COTTON IMPORTER, AND IT DOES NOT APPEAR LIKELY THAT IMPORTS WILL SOON BE REPLACED BY INCREASES IN DOMESTIC PRODUCTION. CURRENT LOWERED FOREIGN DEMAND MAY TEMPORARILY REDUCE THE PRC'S IMPORT

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REQUIREMENTS (THERE IS IN FACT A REPORT THAT THE CHINESE WILL BE EXPORTING SOME COTTON TO JAPAN). BUT OVER THE LONGER TERM, THE US, WITH ITS REPUTATION AS A RELIABLE SOURCE OF SUPPLY, SHOULD CONTINUE TO BE IN A GOOD POSITION AS FAR AS COTTON SALES TO CHINA ARE CONCERNED.

8. SLOW PROGRESS IN US SALES OF PLANT AND EQUIPMENT:

IN CONTRAST TO 1973 WHEN THERE WAS CONSIDERABLE CHINESE PRELIMINARY ACTIVITY WITH US FIRMS (EXPLORATORY TALKS, REQUESTS FOR BIDS, ETC.), COMPARATIVELY LITTLE IN WAY OF FURTHER NEGOTIATIONS TOOK PLACE IN 1974. MOREOVER, ACTUAL PURCHASES OF PLANT, AND OF MACHINERY AND EQUIPMENT FROM THE US WERE MUCH LOWER IN 1974 THAN IN 1973. UNLIKE THE PROBLEMS IN AGRICULTURAL COMMODITIES, THE REASONS FOR SLOW PROGRESS IN NEGOTIATIONS AND SALES OF US INDUSTRIAL GOODS AND TECHNOLOGY ARE DIFFICULT TO PIN DOWN.

9. THE SLOWDOWN IS IN PART ATTRIBUTABLE TO FACTORS WHICH DO NOT IMPLY DISCRIMINATION AGAINST US FIRMS. FOR EXAMPLE, MOST CHINESE PURCHASES OF WHOLE PLANTS IN 1974 HAD LONG BEEN UNDER NEGOTIATION, AND AMERICAN FIRMS HAD NOT BEEN CONSIDERED FROM THE START EITHER BECAUSE OF LACK OF COMMERCIAL CONTACT WHEN THESE NEGOTIATIONS BEGAN OR BECAUSE US FIRMS AT THAT POINT WERE NOT CONSIDERED

COMPETITIVE. ANOTHER POSSIBLE REASON IS THAT CHINESE PURCHASES OF MACHINERY AND EQUIPMENT (OTHER THAN WHOLE PLANTS) ARE BELIEVED TO HAVE DECLINED GENERALLY OVER THE LAST YEAR, AND IF SO, IT MAY BE THAT US FIRMS DID NOT FARE TOO BADLY AFTER ALL. ANOTHER FACTOR IS CHINESE FAMILIARITY OR LONG ASSOCIATION WITH FIRMS IN WESTERN EUROPE AND JAPAN, AND A CONTRASTING LACK OF FAMILIARITY WITH US FIRMS AND WHAT THEY HAVE TO OFFER. THE CONCEPT OF "OLD FRIENDS" IS IMPORTANT TO THE CHINESE, AND THEY OFTEN PREFER TO DEAL WITH COMPANIES WITH WHICH THEY PREVIOUSLY HAD SATISFACTORY RELATIONSHIPS RATHER THAN SWITCH BUSINESS TO NEW FIRMS.

10. SUCH FACTORS NOTWITHSTANDING, WE NONETHELESS FEEL THAT US FIRMS COULD HAVE DONE BETTER, AND THAT THIS WAS NOT DUE TO LACK OF EFFORT ON THEIR PART. WHILE DIFFICULT TO DOCUMENT, WE SUSPECT THAT IN SOME CASES THE CHINESE HAVE INTENTIONALLY LOOKED

AWAY FROM POTENTIAL US SUPPLIERS WHO MIGHT HAVE BEEN ABLE TO  
PROVIDE DESIRED EQUIPMENT AT COMPETITIVE PRICES. (THE  
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FRUSTRATIONS OF GE, AT LEAST UNTIL RECENTLY, MAY BE A CASE IN  
POINT.) WE ALSO KNOW OF A NUMBER OF CASES WHERE THE CHINESE  
INDICATED A PREFERENCE TO DEAL WITH FOREIGN SUBSIDIARIES OF US FIRMS  
RATHER THAN WITH THE PARENT US FIRMS THEMSELVES. (EXAMPLES  
INCLUDE CHINESE NEGOTIATIONS LAST SPRING WITH THE CANADIAN  
SUBSIDIARY OF DRESSER INDUSTRIES FOR OIL EQUIPMENT, RECENT  
DISCUSSIONS WITH LUMMUS FOR AN ETHYLENE PLANT, AND CHINESE  
INDICATIONS TO M.W. KELLOGG OF A PREFERENCE TO DEAL WITH  
KELLOGG'S EUROPEAN SUBSIDIARIES IN REGARD TO CERTAIN ADDITIONAL  
PROJECTS.) THERE HAVE ALSO BEEN A NUMBER OF INSTANCES WHERE  
THE CHINESE HAVE SPECIFIED NON-US SOURCES FOR CERTAIN AMERICAN  
EQUIPMENT AND SUPPLIES THEY WISH TO PURCHASE (E.G. SEE HONG  
KONG 13424).

11. THIS IS NOT TO SAY THAT BUSINESS IS NOT BEING DONE WITH  
US FIRMS. IN CERTAIN CASES PL 1974, THE CHINESE DID NOT  
HESITATE TO DEAL WITH AMERICAN FIRMS. THE WABCO SALE OF  
HEAVY MINING VEHICLES, FOR EXAMPLE, OR THE PURCHASES OF OIL  
EQUIPMENT FROM BAKER TRADING COMPANY. THERE IS ALSO THE RECENT  
INSTANCE OF A POSSIBLE SWITCH FROM POTENTIAL UK SUPPLIERS TO  
AN AMERICAN FIRM, UOP, FOR AN ISOMAR PAREX PLANT THE CHINESE WISH  
TO BUY. THE PICTURE IS BY NO MEANS CLEAR, BUT WE SUSPECT THERE HAS  
BEEN NO HESITATION TO DEAL WITH US FIRMS WHEN ALTERNATIVE  
SOURCES OF SUPPLY ARE NOT AVAILABLE OR WHEN THE US PRODUCT IS  
MARKEDLY SUPERIOR IN QUALITY OR PRICE.

12. IT IS MOST DIFFICULT TO GET AT THE REASONS FOR THE APPARENT  
CHINESE DESIRE TO LOOK, WHEN POSSIBLE, TO OTHER SOURCES OF SUPPLY.  
ONE IS THE IMBALANCE IN SINO-US TRADE, BUT WHILE IT IS  
UNDoubtedly A FACTOR, WE DO NOT FIND IT A SUFFICIENT EXPLANATION.  
THE CHINESE URGE MANY COUNTRIES (E.G. CANADA, AUSTRALIA, WEST  
GERMANY, ETC.) TO TAKE MORE OF THEIR EXPORTS, BUT THEY HAVE NEITHER  
DEMANDED BALANCED TRADE NOR CONDITIONED CHINESE PURCHASES ON  
MORE IMPORTS FROM THE PRC. AT THE TIME USLO WAS ESTABLISHED,  
CHINESE OFFICIALS GAVE US THE IMPRESSION THAT THEY DID NOT  
EXPECT BALANCED TRADE IN THE SHORT RUN, BUT WANTED TO SEE SOME  
PROGRESS ON THEIR SIDE OF THE LEDGER (WHICH THEY HAVE SEEN). ALSO,  
THE CHINESE MUST HAVE REALIZED THAT AN EVENTUAL REDUCTION OF THEIR  
LARGE AGRICULTURAL PURCHASES WOULD DO FAR MORE TO RECTIFY THE  
LARGE IMBALANCE THAN ANY EFFORT TO DIRECT PURCHASES OF EQUIPMENT  
TO NON-US SOURCES. IT MAY BE THAT IT IS THE SIZE OF THE  
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IMBALANCE THAT GIVES THEM A PROBLEM, BUT WE RATHER SUSPECT THAT THE CHINESE ARE LESS DISTURBED BY ITS SIZE THAN BY THE FACT THAT THE IMBALANCE IS WITH THE US, AND HERE POLITICAL FACTORS SEEM TO BE AT PLAY.

13. WE SEE TWO POSSIBLE POLITICAL EXPLANATIONS. ONE PERTAINS TO SINO-US RELATIONS AND A DESIRE ON THE PART OF THE CHINESE, WHETHER OR NOT THERE IS IMPATIENCE WITH THE PACE OF NORMALIZATION, TO DEMONSTRATE THAT AT THE PRESENT LEVEL OF RELATIONS THE US SHOULD NOT EXPECT TO BE TREATED THE SAME AS OTHERS. THERE HAVE BEEN A NUMBER OF STATEMENTS BY CHINESE OFFICIALS OVER THE LAST YEAR, ONE AS RECENT AS A MONTH AGO, THAT TRADE EXCHANGES CANNOT FULLY DEVELOP PRIOR TO POLITICAL NORMALIZATION, AND WE PRESUME THAT PRONONCMENTS SUCH AS THESE MUST AT SOME POINT BE TRANSLATED INTO CONCRETE DECISIONS. ONE WAY TO DO THIS IS TO LOOK AWAY FROM US FIRMS, WHICH ARE MOST ANXIOUS TO BEGIN SELLING TO THE CHINESE. ANOTHER, IS TO GO SLOW ON SUCH MATTERS AS TRADE MISSIONS AND EXHIBITS, WHICH MANY AMERICANS SEE AS IMPORTANT VEHICLES FOR PENETRATING THE CHINESE MARKET. IF THIS IS THE CHINESE OBJECTIVE, THEY HAVE TO SOME EXTENT SUCCEEDED, FOR AN INCREASING NUMBER OF US FIRMS AND TRADE ORGANIZATIONS ATTRIBUTE THEIR LACK OF PROGRESS WITH THE PRC TO THE PRESENT STATE OF BILATERAL POLITICAL RELATIONS. IT MAY ALSO BE THAT THROUGH SUCH TACTICS THE CHINESE HOPE TO GENERATE SUPPORT FOR THE EVENTUAL GRANTING OF MFN TO THE PRC, WHICH THEY PROBABLY SEE AS AN INTEGRAL PART OF NORMALIZATION.

14. THE OTHER POSSIBLE POLITICAL EXPLANATION STEMS FROM THE APPARENT INCONSISTENCY ON THE ONE HAND, BETWEEN CHINA'S TRADE WITH THE US AND, ON THE OTHER HAND, ITS RELENTLESS CRITICISM OF THE US AS A SUPERPOWER, ITS BID FOR LEADERSHIP OF THE THIRD WORLD, AND ITS PRINCIPLED ADHERENCE TO SELF-RELIANCE -- ALL OF WHICH WERE GIVEN GREAT STRESS IN 1974. THE RAPID GROWTH OF SINO-US TRADE, WHICH SUDDENLY MADE THE US CHINA'S SECOND LARGEST TRADE PARTNER, AND THE GREAT IMBALANCE OF THAT TRADE, WHICH VERY CLEARLY WAS DUE TO CHINA'S NEED FOR AGRICULTURAL COMMODITIES, MIGHT HAVE BEEN VERY DIFFICULT FOR THE PRC TO RECONCILE WITH ITS BROAD POLITICAL AND IDEOLOGICAL POSTURE. THUS AN ATTEMPT TO SLOW DOWN THE RAPID GROWTH OF TRADE RELATIONS WITH THE US, AND PERHAPS A SIGH OF RELIEF WHEN IMPROVED AGRICULTURAL PROSPECTS MADE IT POSSIBLE TO PARE DOWN PURCHASES OF US AGRICULTURAL COMMODITIES.

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15. IN THE CONTEXT OF THIS SECOND POLITICAL REASON, THE PROBLEM TO THE CHINESE OF THE TRADE IMBALANCE IS PERHAPS MORE UNDERSTANDABLE. IT IS ALSO CONCEIVABLE THAT A SHORT DECLINE IN AGRICULTURAL IMPORTS FROM THE US IN 1975, WHICH WOULD LOWER THE LEVEL OF OVERALL TRADE AND TO SOME EXTENT IMPROVE THE BILATERAL BALANCE, COULD BE ACCCOMPANIED BY INCREASED CHINESE PURCHASES OF AMERICAN EQUIPMENT AND TECHNOLOGY. WE WONDER WHETHER THE RECENT REVIVAL INTEREST IN A VARIETY OF UOP PROPOSALS, AND THE CURRENT TECHIMPORT VISIT TO GE, WESTINGHOUSE, AND DRESSER INDUSTRIES IN THE US, MIGHT NOT SIGNAL SUCH A CHANGE.

16. OVER THE LONG TERM THERE IS VERY LARGE POTENTIAL FOR US SALES OF PLANT, MACHINERY AND TECHNOLOGY TO CHINA, AND WE HAVE SEEN NOTHING IN PEKING TO CONTRADICT OUR FEELINGS OF CONSIDERABLE CHINESE INTEREST IN WHAT THE US CAN OFFER. WE SUSPECT THAT WERE IT NOT FOR THE INHIBITIONS REGARDING DEALINGS WITH US FIRMS ALLUDED TO ABOVE, OUR SALES IN THIS AREA WOULD RISE MORE RAPIDLY. WHILE WE WOULD NOT ADVOCATE POLITICAL CONCESSIONS TO SECURE A GREATER SHARE OF PRC FOREIGN TRADE, WE BELIEVE THE CHINESE ARE SERIOUS WHEN THEY SAY THAT FULL TRADE RELATIONS CANNOT DEVELOP UNTIL POLITICAL RELATIONS ARE NORMALIZED. AT THE SAME TIME, THE US SHOULD BE PREPARED IN ANY FUTURE NEGOTIATIONS, FOR EXAMPLE

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IN CONNECTION WITH MFN, TO SEEK NON-DISCRIMINATORY ACCESS FOR US FIRMS TO THE CHINA MARKET.

17. "ATMOSPHERICS" OF TRADE: IN NOVEMBER 1973, A DELEGATION OF THE NATIONAL COUNCIL FOR US-CHINA TRADE (NCUSCT) -- PROMINENTLY BILLED BY THE US AS THE FIRST AMERICAN TRADE DELEGATION TO CHINA IN 25 YEARS -- REACHED AGREEMENT IN PEKING FOR A RETURN VISIT OF A CCPIT DELEGATION TO THE US IN 1974, AND AGREEMENT IN PRINCIPLE FOR SUBSEQUENT EXCHANGES OF TRADE MISSIONS AND EXHIBITIONS. HOWEVER, LITTLE FURTHER PROGRESS HAS BEEN MADE SINCE. THE CCPIT VISIT WAS POSTPONED BECAUSE THE CHINESE WERE "TOO BUSY," THOUGH IT IS NOW EXPECTED TO TAKE PLACE IN 1975. THE CHINESE HAVE ALSO SPURNED ALL OF THE VERY LARGE NUMBER OF PROPOSALS FOR TRADE MISSIONS AND DELEGATIONS THAT HAVE BEEN MADE BY VARIOUS TRADE, INDUSTRIAL, STATE, AND CIVIC ORGANIZATIONS. IF A REASON IS HINTED AT BY THE CHINESE, IT IS TO THE EFFECT THAT POLITICAL CONDITIONS ARE NOT RIGHT.

18. IN THIS AREA OF "ATMOSPHERICS" THE CHINESE ARE DEMONSTRATING UNAMBIGUOUSLY THAT TRADE EXCHANGES CANNOT FULLY DEVELOP UNTIL NORMALIZATION. TRADE MISSIONS ARE RELATIVELY HIGH VISIBILITY ACTIVITIES WITH LITTLE SIGNIFICANT EFFECT ON TRADE IN THE SHORT TERM. WHILE THE CHINESE WOULD UNDOUBTEDLY BENEFIT FROM SUCH MISSIONS, PARTICULARLY THOSE WHICH WOULD PROMOTE OR FACILITATE PRC EXPORTS TO THE US, THEY PROBABLY SEE THESE TYPES OF ACTIVITIES IN GENERAL AS PRIMARILY SOMETHING THE AMERICANS WANT FOR THEIR OWN PURPOSES.

19. IN ANY EVENT, THE CHINESE IN ADDITION TO MAINTAINING FRIENDLY CONTACT WITH THE NCUSCT, HAVE SOUGHT TO BROADEN THEIR CONTACTS AMONG THOSE ORGANIZATIONS WHICH WISH TO PROMOTE SINO-US TRADE, SUCH AS THE AMERICAN IMPORTERS ASSOCIATION AND THE AMERICAN CHAMBER OF COMMERCE IN HONG KONG, WHICH HAVE BEEN INVITED TO PEKING AND THE CANTON FAIRS. WITH LITTLE EFFORT ON THEIR PART, THE CHINESE ARE WINNING A CONSTITUENCY OF GROUPS WHICH VIGOROUSLY FAVOR NORMALIZATION, EXPANSION OF TRADE, MFN FOR CHINA, ETC.

20. THE TECHIMPORT DELEGATION THAT IS NOW VISITING VARIOUS FIRMS IN THE US DOES NOT FALL IN OUR CONCEPT OF "ATMOSPHERICS." IT IS RATHER A LOW VISIBILITY TECHNICAL GROUP, GEARED TO VERY SPECIFIC CONFIDENTIAL

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INTERESTS, THOUGH IT MAY IN FACT HAVE SIGNIFICANT TRADE EFFECTS.

21. PROBLEM OF STEEL SCRAP: THE PROBLEM OF STEEL SCRAP IS DIFFERENT FROM MOST OTHER PROBLEMS IN SINO-US TRADE, EXCEPT

INSOFAR AS IT ILLUSTRATES HOW RIGID CHINESE ADHERE TO "PRINCIPLE" CAN BE. THE CHINESE APPARENTLY NEEDED THE 500 THOUSAND TONS WHICH THEY ORDERED BUT WHICH COULD NOT BE DELIVERED DUE TO USG EXPORT CONTROLS. YET THEY REFUSED TO TAKE THAT SCRAP (PERHAPS 200 THOUSAND TONS OVER THE YEAR) WHICH THEY MIGHT HAVE OBTAINED BY WORKING WITHIN THE FRAMEWORK OF THE PROGRAM. THEY MAY HAVE FELT THAT TO DO SO WOULD UNDERMINE THEIR POSITION THAT THE UNFULFILLED CONTRACTS WERE STILL VALID, BUT THEY MAY ALSO HAVE BEEN SENSITIVE ABOUT COMPLYING WITH USG REGULATIONS WHICH, IN THEIR VIEW, IMPINGE ON THEIR COMMERCIAL RELATIONSHIPS WITH PRIVATE FIRMS. SCRAP HAS GOOD LONG

TERM POTENTIAL AS A US EXPORT TO CHINA, AND WITH EXPORT CONTROLS NOW LIFTED, WE SHOULD BE ALERT FOR OPPORTUNITIES TO FOSTER AN ORDERLY RESUMPTION OF THIS TRADE.

22. PUSH ON CHINESE EXPORTS TO THE US: WE BELIEVE THERE HAS BEEN A SERIOUS CHINESE EFFORT TO INCREASE EXPORTS TO THE US. OUR IMPORTS FROM CHINA EXCEEDED EXPECTATIONS IN 1974, AND MAY HAVE REACHED \$120 MILLION, COMPARED TO \$64 MILLION IN 1973. IN 1975, IT MIGHT GO TO \$160 MILLION OR HIGHER.

23. THE CHINESE EXPORT EFFORT IS REFLECTED IN THE LARGE NUMBER OF NEW POTENTIAL AMERICAN IMPORTERS THEY HAVE INVITED TO EACH CANTON FAIR, THEIR WILLINGNESS TO INVITE THOSE WITH GOOD LONG TERM PROSPECTS TO VISIT CHINA BETWEEN THE FAIRS, AND AN IMPROVEMENT, ALBEIT SLOW, IN MEETING IMPORTER REQUIREMENTS ON SUCH MATTERS AS LABELLING, SHRINKAGE, STYLING, ETC.

24. AT THE SAME TIME, THERE ARE MANY FRUSTRATIONS AND DISAPPOINTMENTS AMONG AMERICAN BUYERS. FOR EXAMPLE, MANY FAIR VISITORS FIND THE CHINESE UNRESPONSIVE OR THE OPPORTUNITIES OTHERWISE LIMITED, AND DON'T SUBSEQUENTLY RETURN TO CANTON. NEVERTHELESS, THERE IS A GENERAL UPWARD TREND IN SALES TO THE US, AND NEW IMPORTANT ITEMS CONTINUE TO APPEAR, SUCH AS THE LARGE CONTRACTS FOR TIN AND TUNGSTEN THIS LAST FALL.

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25. IF THE CHINESE WERE MORE WILLING TO COMPLY WITH USG IMPORT REQUIREMENTS-- FOR EXAMPLE, THE PROBLEM OF FDA REJECTION OF FROZEN SHRIMP -- THERE WOULD BE SIGNIFICANT POTENTIAL FOR FURTHER EXPORTS TO THE US. AT THE MOMENT, MANY CHINESE TRADE OFFICIALS STILL BELIEVE THAT PROBLEMS OF THIS SORT CONCERN NOT CHINA, BUT RATHER THE IMPORTER AND HPS GOVERNMENT. WE THINK THERE IS SOME SLOW CHANGE IN THIS ATTITUDE.

26. THE CHINESE ARE ACUTELY ANXIOUS OF THE PROBLEMS PRESENTED BY THE LACK OF MFN. WHILE THEY AGAIN TAKE THE POSITION THAT IT IS A "US PROBLEM," THEY ALLUDE TO THE ABSENCE OF MFN WITH US AT THE WORKING LEVEL AND IN CONVERSATIONS WITH ALMOST ALL

AMERICAN IMPORTERS. THERE IS NO DOUBT IN OUR MINDS THAT IT IS SOMETHING THEY WANT, AND PROBABLY EXPECT, AS A PART OF THE NORMALIZATION PROCESS. WE ARE NOT SO CONFIDENT, HOWEVER, THAT THEY HAVE A PERCEPTION OF THE DIFFICULTIES THAT NEGOTIATIONS FOR MFN MAY ENTAIL.

27. WORKING FROM A STILL RELATIVELY LOW BASE, CHINESE EXPORTS TO THE US SHOULD CONTINUE TO SHOW GOOD PERCENTAGE INCREASES, BUT BARRING A DRASTIC CURTAILMENT OF PURCHASES FROM THE US, THE TRADE IMBALANCES SHOULD REMAIN LARGE OVER THE FORSEEABLE FUTURE. SHOULD SOME HIGH VOLUME, HIGH VOLUME COMMODITY - SUCH AS OIL - BECOME A PART OF THIS TRADE, THE PICTURE COULD CHANGE.

HOLDRIDGE

CONFIDENTIAL

NNN

## Message Attributes

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